

Report of the auditor-general to the Eastern Cape provincial legislature and the council on Lukhanji Local Municipality

Report on the financial statements

Introduction

1. I have audited the financial statements of the Lukhanji Local Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2015, the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget and actual amounts for the year then ended, as well as the notes, comprising a summary of significant accounting policies and other explanatory information.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with South African Standards of Generally Recognised Accounting Practice (SA standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2014 (Act No. 10 of 2014) (DoRA), and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-general's responsibility

3. My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with International Standards on Auditing. Those standards require that I comply with ethical requirements, and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the municipality's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the municipality's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified audit opinion.

Basis for qualified opinion

Property, plant and equipment

6. The municipality did not account for its PPE in accordance with GRAP 17, Property, plant and equipment in the following circumstances:
 - The municipality did not record all of its assets in the fixed asset register and financial statements;
 - The municipality made errors in the calculation of depreciation and work-in-progress.
7. Consequently, PPE as disclosed in note 10 is understated by R109 million (2014: R109,6 million), depreciation as disclosed on the statement of financial performance is overstated by R2,4 million (2014: R1,6 million) and accumulated surplus as disclosed in the statement of financial position is understated by R106,7 million (2014: R108 million).
8. In addition I was unable to obtain sufficient appropriate audit evidence for PPE as I was not provided with sufficient appropriate evidence for journals relating to PPE.
9. I was unable to confirm the amount of PPE by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to property, plant & equipment of R758,1 million as disclosed in note 10 to the financial statements.

Investment property

10. The municipality did not account for its investment properties in accordance with GRAP 16 Investment property the following circumstances
 - Properties could not be physically located as the municipality did not prepare a register that was fully compliant with the requirements of GRAP;
 - Ownership control of properties included on the register could not be confirmed;
 - The municipality made errors in the calculation of the cost of properties;
 - The municipality did not record all of its properties on the register;
 - The register did not contain adequate details of buildings and improvements on the properties recorded.
11. Consequently, investment property as disclosed in note 9 is understated by R49,5 million (2014: R49,5 million) and accumulated surplus as disclosed in the statement of financial position is understated by R49,5 million (2014: R49,5 million). The municipality did not calculate depreciation on buildings included in investment property, in contravention of the accounting policy. As insufficient details were included on the register it is impracticable to determine the impact of the error on depreciation.

Irregular expenditure

12. Irregular expenditure of R166,8 million (2014: R107,8 million) is disclosed in note 53. The municipality's processes for the recording and recognition of irregular expenditure were insufficient as amounts either did not agree to supporting documentation or were not recorded. Consequently, irregular expenditure is understated by R10,4 million (2014: R16 million).
13. In addition I was unable to obtain sufficient appropriate audit evidence for the irregular expenditure balance brought forward from the prior year and the prior year closing balance of irregular expenditure as disclosed at R107,8 million in note 53 as I was not provided with appropriate documentation to substantiate the amount disclosed. I was unable to confirm the amount of irregular expenditure by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to irregular expenditure of R166,8 million (2014: R107,8 million) as disclosed in note 53 to the financial statements.

Revenue from exchange transactions

14. The municipality did not account for revenue from exchange transactions in accordance with GRAP 9, Revenue from exchange transactions in the following circumstances:
- The municipality made errors in the calculation of meter readings for service charges;
 - The municipality did not record interest transactions in the correct period;
 - Calculation errors, including Value Added Tax (VAT) errors were made on recording of other income;
 - Revenue was recognised that did not meet the recognition criteria.
15. Consequently, revenue from exchange transactions as disclosed in the statement of financial performance, is overstated by R31 million and receivables from exchange transactions is overstated by R12,3 million, expenditure is overstated by R17,7 million, employee costs is overstated by R360 681 and VAT is understated by R752 088.
16. In addition I was unable to obtain sufficient appropriate audit evidence for revenue from exchange transactions because I was not provided with sufficient appropriate evidence for revenue transactions.
17. I was unable to confirm the amount of revenue from exchange transactions by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to revenue from exchange transactions of R252,9 million as disclosed in the statement of financial performance.

Discontinued operations

18. Disclosed in note 40 for discontinued operations, are receivables from exchange transactions of R15 million. The municipality did not account for these appropriately as:

- Appropriate records to support the debtor balance were not kept by the municipality;
- The municipality did not calculate the impairment related to these receivables correctly.

19. Consequently, receivables relating to discontinued operations as disclosed in note 40 is understated by R15,8 million.

Unauthorised expenditure

20. I was unable to obtain sufficient appropriate audit evidence for the opening balance and corresponding amount for unauthorised expenditure of R78,8 million as management does not have appropriate systems to identify this expenditure.
21. I was unable to obtain the required evidence through alternative means. Consequently, I was unable to determine whether any adjustments to corresponding amount for unauthorised expenditure of R2,9 million as disclosed in note 51 to the financial statements were necessary.
22. Management does not have appropriate systems to identify this expenditure and, consequently, R27,1 million (2014: R27,1 million) of unauthorised expenditure that was detected during the audit process was not disclosed in note 51.

Aggregation of immaterial uncorrected misstatements

23. The financial statements were materially misstated due to the cumulative effect of numerous individually immaterial uncorrected misstatements in the following items included in the statement of financial position, the statement of financial performance and the notes to the financial statements:
- The corresponding figure of employee costs reflected as R128,9 million was overstated by R4,8 million.
 - The corresponding figure for revenue from non-exchange transactions reflected as R235,7 million was understated by R11,2 million.
 - Receivables from exchange transactions reflected as R24,4 million (2014: R21,3 million) was understated by R3,8 million (2014: 12,5 million).
 - VAT receivable reflected as R4,4 million was understated by R7,6 million.
 - Accumulated surplus reflected as R1,1 billion was understated by R21,7 million.
 - Receivables from non-exchange reflected as R38,1 million was understated by R5,7 million.
24. In addition, I was unable to obtain sufficient appropriate audit evidence and to confirm the following items by alternative means:
- The corresponding figure of employee costs of R7,5 million as included in the disclosed balance of R128,9 million.

- The corresponding figure of revenue from non-exchange transactions of R1,4 million as included in the disclosed balance of R235,7 million.
- Receivables from exchange transactions of R648 000 (2014: R648 024) as included in the balance of R24,4 million (2014: R21,3 million).
- Unspent grant liability of R1,3 million (2014: R9,4 million) as included in the disclosed balance of R14,6 million (2014: R9,5 million).
- Accumulated surplus of R239 827 as included in the disclosed balance of R1,1 billion.

25. Consequently, I was unable to determine whether any further adjustment to these items was necessary.

Qualified opinion

26. In my opinion, except for the effects of the matters described in the basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of the Lukhanji Local Municipality as at 30 June 2015 and its financial performance and cash flows for the year then ended, in accordance with SA standards of GRAP and the requirements of the MFMA and DoRA.

Emphasis of matters

27. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Restatement of corresponding figures

28. As disclosed in the statement of changes in net assets and note 47, the corresponding figures for have been restated as a result of errors only corrected during the year ended 30 June 2015 that existed in the financial statements at, and for the year ended 30 June 2014.

Material impairments

29. As disclosed in note 4 and 5 to the financial statements, an amount of R222,7 million for receivables from exchange transactions and R75 million for receivables from non-exchange transactions (2014: R222,5 million and R92,5 million) has been impaired as a result of non-payment of consumer debtor accounts.

Additional matter

30. I draw attention to the matter below. My opinion is not modified in respect of this matter.

Unaudited disclosure notes

31. In terms of section 125(2) (e) of the MFMA, the municipality is required to disclose particulars of non-compliance with this legislation. This disclosure requirement did

not from part of the audit of the financial statements and accordingly I do not express an opinion thereon.

Report on other legal and regulatory requirements

32. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof, I have a responsibility to report findings on the reported performance information against predetermined objectives for selected development priorities presented in the annual performance report, compliance with legislation and internal control. The objective of my tests was to identify reportable findings as described under each subheading, but not to gather evidence to express assurance on these matters. Accordingly, I do not express an opinion or conclusion on these matters.

Predetermined objectives

33. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the following selected development priorities presented in the annual performance report of the municipality for the year ended 30 June 2015:
- Development priority: basic services and infrastructure development on pages x to x
 - Development priority: local economic development on pages x to x
34. I evaluated the reported performance information against the overall criteria of usefulness and reliability.
35. I evaluated the usefulness of the reported performance information to determine whether it was presented in accordance with the National Treasury's annual reporting principles and whether the reported performance was consistent with the planned development priorities. I further performed tests to determine whether indicators and targets were well defined, verifiable, specific, measurable, time bound and relevant, as required by the National Treasury's *Framework for managing programme performance information* (FMPPI).
36. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
37. The material findings in respect of the selected development priorities are as follows:

Basic services and infrastructure development

Usefulness of reported performance information

38. Section 41(c) of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA) requires actual achievements against all planned indicators and targets to be reported annually. The annual performance report submitted for audit purposes did not include the actual performance of 100% of all planned objectives specified in the integrated development plan (IDP) for the year under review. This was due to a lack of information systems recording and documenting actual achievements against targets and a lack of review of the completeness of reporting documents by management and the internal audit unit.

39. Section 54(1)(c) of the MFMA determines that the service delivery and budget implementation plan adopted by the municipal council may be amended only if the council approves an adjustments budget. Changes to the service delivery and budget implementation plan in the year have to be made in accordance with the process as prescribed per section 28 of the MFMA. Material changes were made to the development priorities, objectives, indicators and targets in the annual performance report, without following the process as prescribed in section 28 of the MFMA and or without adoption by the municipal council. This was as a result of management not developing appropriate measures to monitor compliance with applicable law and regulations. Management has also not created and implemented action plans that address deficiencies identified by external auditors.
40. The FMPPi requires the following:
41. Performance targets must be specific in clearly identifying the nature and required level of performance and must be measurable and the period or deadline for delivery of targets must be specified.
42. Performance indicators must be well defined by having clear data definitions so that data can be collected consistently and is easy to understand and use. Performance indicators must also be verifiable.
43. The measurability of planned targets and indicators could not be assessed due to a lack of technical indicator descriptions and proper systems and processes and formal standard operating procedures or documented system descriptions.
44. The FMPPi requires indicators to relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives. The relevance of the indicators could not be assessed due to a lack of corroborative supporting evidence to verify management's explanation why the indicators were considered important and relevant to the realisation of strategic goals and objectives.

Reliability of reported performance information

45. The FMPPi requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. We were unable to obtain the information and explanations we considered necessary to satisfy ourselves as to the reliability of the reported performance information. This was due to limitations placed on the scope of our work due to the fact that the auditee could not provide sufficient appropriate evidence in support of the reported performance information and the auditee's records did not permit the application of alternative audit procedures.

Local economic development

Usefulness of reported performance information

46. Section 41(c) of the MSA requires actual achievements against all planned indicators and targets to be reported annually. The annual performance report submitted for audit purposes did not include the actual performance of 100% of all planned objectives specified in the integrated development plan (IDP) for the year under review. This was due to a lack of information systems recording and documenting

actual achievements against targets and a lack of review of the completeness of reporting documents by management and the internal audit unit.

47. Section 54(1)(c) of the MFMA determines that the service delivery and budget implementation plan adopted by the municipal council may be amended only if the council approves an adjustments budget. Changes to the service delivery and budget implementation plan in the year have to be made in accordance with the process as prescribed per section 28 of the MFMA. Material changes were made to the development priorities, objectives, indicators and targets in the annual performance report, without following the process as prescribed in section 28 of the MFMA and or without adoption by the municipal council. This was as a result of management not developing appropriate measures to monitor compliance with applicable law and regulations. Management has also not created and implemented action plans that address deficiencies identified by external auditors.
48. The FMPPI requires the following:
49. Performance targets must be specific in clearly identifying the nature and required level of performance and must be measurable and the period or deadline for delivery of targets must be specified.
50. Performance indicators must be well defined by having clear data definitions so that data can be collected consistently and is easy to understand and use. Performance indicators must also be verifiable.
51. The measurability of planned targets and indicators could not be assessed due to a lack of technical indicator descriptions and proper systems and processes and formal standard operating procedures or documented system descriptions.
52. The FMPPI requires indicators to relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives. The relevance of the indicators could not be assessed due to a lack of corroborative supporting evidence to verify management's explanation why the indicators were considered important and relevant to the realisation of strategic goals and objectives.

Reliability of reported performance information

53. The FMPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. We were unable to obtain the information and explanations we considered necessary to satisfy ourselves as to the reliability of the reported performance information. This was due to limitations placed on the scope of our work due to the fact that the auditee could not provide sufficient appropriate evidence in support of the reported performance information and the auditee's records did not permit the application of alternative audit procedures.

Additional matters

54. I draw attention to the following matters, my opinion is not modified in respect of these matters:

Achievement of planned targets

55. Refer to the annual performance report on pages x to x and x to x for information on the achievement of the planned targets for the year. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information for the selected development priorities reported in paragraphs 38 to 53 of this report.

Unaudited supplementary information

56. The supplementary information set out on pages XX to XX does not form part of the annual performance report and is presented as additional information. I have not audited these schedules and, accordingly, I do not report thereon.

Compliance with legislation

57. I performed procedures to obtain evidence that the municipality had complied with applicable legislation regarding financial matters, financial management and other related matters. My material findings on compliance with specific matters in key legislation, as set out in the general notice issued in terms of the PAA, are as follows:

Audit committee

58. An audit committee was not in place, as required by section 166(1) of the MFMA and consequently the municipality did not comply with any of the requirements of the MFMA and municipal planning and performance regulations applicable to audit committees.
59. A performance audit committee was not in place and there was no audit committee to fulfil the performance audit committee function, as required by Municipal planning and performance management regulation 14(2)(a).

Internal audit

60. An internal audit unit was not established, as required by section 165(1) of the MFMA.
61. The internal audit unit did not function as required by section 165(2) of the MFMA, in that:
- it did not advise the accounting officer on matters relating to internal audit, internal controls, accounting procedures and practices and risk and risk management.
 - it did not advise the accounting officer on matters relating to compliance with the MFMA, the DoRA and other applicable legislation, as required by section 165(2)(b)(vii) of the MFMA.

Expenditure management

62. Payments were made from the municipality's bank account without the approval of a properly authorised official, as required by section 11(1) of the MFMA.

63. An effective system of expenditure control, including procedures for the approval of funds, was not in place, as required by section 65(2)(a) of the MFMA.
64. An adequate management, accounting and information system was not in place which recognised expenditure when it was incurred, accounted for creditors and accounted for payments made, as required by section 65(2)(b) of the MFMA.
65. Reasonable steps were not taken to prevent unauthorised expenditure, irregular expenditure and fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.

Revenue Management

66. A credit control and debt collection policy was not implemented, as required by section 96(b) of the MSA and section 62(1)(f)(iii) of MFMA.
67. An effective system of internal control for revenue was not in place, as required by section 64(2)(f) of the MFMA.

Asset Management

68. An effective system of internal control for assets (including an asset register) was not in place, as required by section 63(2)(c) of the MFMA.
69. The municipality did not establish an investment policy that was adopted by council, as required by section 13(2) of the MFMA and Municipal investment regulation 3(1)(a) and 3(2).

Liability Management

70. An adequate management, accounting and information system which accounts for liabilities was not in place, as required by section 63(2)(a) of the MFMA.
71. An effective system of internal control for liabilities (including a liability register) was not in place, as required by section 63(2)(c) of the MFMA.

Consequence Management

72. Unauthorised, Irregular, Fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(a)(ii) of the MFMA.
73. Unauthorised, irregular, fruitless and wasteful expenditure was not always recovered from the liable person, as required by section 32(2) of the MFMA.

Conditional grants

74. The municipality did not evaluate its performance in respect of programmes funded by the Municipal Infrastructure Grant allocation, as required by section 12(5) of the DORA.

75. The municipality did not evaluate its performance in respect of programmes or functions funded by the Municipal Systems Improvement Grant allocation, as required by section 12(5) of the DORA.

Procurement and contract management

76. Sufficient appropriate audit evidence could not be obtained that all contracts and quotations were awarded in accordance with the legislative requirements and a procurement process which is fair, equitable, transparent and competitive, as no service level agreement could be produced by the municipality.
77. Goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations as required by SCM regulation 17(a) & (c).
78. Sufficient appropriate audit evidence could not be obtained that bid specifications for procurement of goods and services through competitive bids were drafted in an unbiased manner that allowed all potential suppliers to offer their goods or services, as per required by SCM regulation 27(2)(a).
79. Sufficient appropriate audit evidence could not be obtained that bid specifications were drafted by bid specification committees which were composed of one or more officials of the municipality as required by SCM regulation 27(3).
80. Bids were not always evaluated by bid evaluation committees which were composed of officials from the departments requiring the goods or services.
81. Sufficient appropriate audit evidence could not be obtained that bid adjudication was always done by committees which were composed in accordance with SCM regulation 29(2).
82. Sufficient appropriate evidence could not be obtained to determine whether there were any recommendations that were made by adjudication committee that are different from evaluation committee that were submitted to the accounting officer first.
83. Sufficient appropriate evidence could not be obtained to determine whether there were any councillors of the municipality that participated in committees evaluating or approving tenders/quotations or that attended meetings of committees evaluating or approving tenders/quotations, in contravention of section 117 of the MFMA.
84. Contracts and quotations were awarded to bidders that did not score the highest points in the evaluation process, as required by section 2(1)(f) of Preferential Procurement Policy Framework Act, 2000 (Act No. 5 of 2000) (PPFA).
85. Contracts and quotations were awarded to bidders based on preference points that were not allocated and calculated in accordance with the requirements of the PPFA and its regulations.
86. Contracts and quotations were awarded to bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, as required by SCM regulation 13(c).
87. Construction contracts were awarded to contractors that were not registered with the Construction Industry Development Board (CIDB) and did not qualify for the contract,

in accordance with section 18(1) of the CIDB Act and CIDB regulations 17 and 25(7A).

88. Sufficient appropriate audit evidence could not be obtained that contracts were only extended or modified after tabling the reasons for the proposed amendment in the council of the municipality as required by section 116(3) of the MFMA.
89. Sufficient appropriate audit evidence could not be obtained that all extension or modification to contracts were approved by a properly delegated official, as required by SCM Regulation 5.
90. The performance of contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA.
91. Sufficient appropriate evidence could not be obtained to determine whether the contract performance and monitoring measures and methods were sufficient to ensure effective contract management, as required by section 116(2)(c) of the MFMA.
92. Sufficient appropriate evidence could not be obtained to determine whether measures to combat the abuse of the SCM system were implemented as per the requirements of SCM regulation 38(1), to ensure that awards are not made to providers who:
 - during the last five years, failed to perform satisfactorily on a previous contract with the municipality or municipal entity or other organ of state;
 - committed a corrupt or fraudulent act in competing for the contract;
 - abused the SCM system of the municipality;
 - had been convicted of fraud or corruption during the past five years.

Annual financial statements, performance and annual reports

93. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA.
94. Material misstatements identified by the auditors in the submitted financial statements were not adequately corrected and the supporting records could not be provided subsequently, which resulted in the financial statements receiving an qualified audit opinion.
95. The oversight report, containing comments on the annual report, was not adopted by council within two months from the date on which the 2013/14 annual report was tabled, as required by section 129(1) of the MFMA.
96. The annual performance report for the year under review did not include
 - the performance of the municipality and
 - a comparison of the performance with set targets and a comparison with the previous financial year and

- measures taken to improve performance, as required by section 46 (1)(a), (b) and (c) of the MSA.

Human Resource management

97. The municipal manager and senior managers directly accountable to the municipal manager did not sign performance agreements, as required by section 57(2)(a) of the MSA.
98. The competencies of financial and supply chain management officials were not assessed in a timely manner in order to identify and address gaps in competency levels as required by Municipal Regulations on Minimum Competency Levels 13.
99. The annual report of the municipality did not reflect information on compliance with prescribed minimum competencies as required by the Municipal Regulations on Minimum Competency Levels 14(2)(b)/14(3).

Strategic and performance management

100. The municipality did not give effect to its IDP and conduct its affairs in a manner which was consistent with its IDP, as required by section 36 of the MSA, section 21(2)(a) of the MFMA and Municipal planning and performance management regulation 6.
101. The IDP was not annually reviewed based on the assessment of its performance measurements and changing circumstances, as required by section 34 of the MSA and Municipal planning and performance management regulation 3 and 11.
102. Key performance indicators, including input, output and outcome indicators, in respect of each of the development priorities and objectives were not set out in the IDP, as required by section 41(1)(a) of the MSA and the Municipal planning and performance management regulation 1 and 9(1)(a).
103. Measurable performance targets for the financial year were not set in the IDP, for each of the key performance indicators and with regard to each of the development priorities or objectives, as required by section 41(1)(b) of the MSA and the Municipal planning and performance management regulations 12(1) and 12(2)(e).
104. The KPIs set by the municipality did not include indicators on percentage of households with access to basic level of electricity and solid waste removal were not set by the municipality as required by section 43(2) of the MSA and the Municipal planning and performance management regulation 10(a).
105. The service delivery and budget implementation plan (SDBIP) for implementing the municipality's delivery of municipal services and annual budget did not indicate projections for each month of the revenue to be collected, by source and/or the operational and capital expenditure, by vote.
106. Sufficient appropriate audit evidence could not be obtained that revisions to the service delivery and budget implementation plan were approved by the council after the approval of the adjustments budget, as required by section 54(1)(c) of the MFMA.
107. The performance of the municipality was not assessed during the first half of the financial year, as required by section 72(1)(a)(ii) of the MFMA.

108. Annual performance agreements for the municipal manager and all senior managers linked to the measurable performance objectives approved with the budget and to the service delivery budget implementation plan were not signed as required in terms of section 53(1)(c)(iii) of the MFMA and section 57(1)(b) of the MSA.
109. The performance management system and related controls were not in place as it did not describe and represent the processes of performance planning, monitoring, measurement, review, reporting, improvement and how it is conducted, organised and managed, including determining the roles of the different role-players, as required by sections 38 of the MSA and regulation 7 of the Municipal planning and performance management regulations.

Internal control

110. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with legislation. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for qualified opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report.

Leadership

111. Leadership did not fulfil its oversight responsibilities with regards to the implementation and monitoring of internal controls and compliance with laws and regulations and did not insist on daily disciplines to ensure sound financial and performance management and compliance with laws and regulations.
112. Critical vacancies were only filled towards the end of the financial year which led to insufficient capacity to address the repeat control deficiencies.

Financial and performance management

113. The municipality's system of internal control did not identify the numerous misstatements within the financial statements. The control environment at the municipality is not fully functional, with inadequate daily, monthly processing and reconciliation of transactions expenditure, employee costs and non-current assets. In addition, management relied on consultants to compile the financial statements at year-end; however the underlying records had various deficiencies.
114. The annual performance reports also included material misstatements due to the lack of oversight of the collection, collation and reporting of performance information. There is limited assurance and accountability over the performance management system.

Governance

115. Risk management activities were not sufficient as evidenced by the large number of repeat findings. The municipality also lacked effective risk monitoring processes in order to ensure risks identified are appropriately managed.
116. The internal audit function lacked sufficient capacity to function effectively and produce reports during the financial year. The audit committee was not properly

constituted and was disbanded during the year. As a result the governance structures of the municipality were severally compromised.

Auditor - General

East London

30 November 2015



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence